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SENATE BILL 2295 By
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HOUSE BILL 2879
By Garrett

AN ACT to amend Tennessee Code Annotated, Title 67, relative to the franchise and excise taxation of real estate investment trusts and related entities.

BE IT ENACTED BY THE GENERAL ASSEMBLY OF THE STATE OF TENNESSEE:

SECTION 1. Tennessee Code Annotated, Section 67-4-2004, is amended by adding the following new subdivisions thereto:

() "Pass-through entity" means an S corporation, an entity treated as a partnership for federal income tax purposes, an entity treated as a trust for federal income tax purposes or a business entity which has a single owner and which is disregarded as an entity separate from its owner for federal income tax purposes, but not for purposes of Parts 20 and 21 of this chapter;

() "Real estate investment trust" means an entity which has an election in effect under Section 856(c)(i) of the Internal Revenue Code;

SECTION 2. Tennessee Code Annotated, Section 67-4-2006(b)(1), is amended by deleting item (I) in its entirety and by substituting instead the following new items:

(I) Any net loss or any item of expense or loss which meets all of the following criteria:

- (i) Is included in the determination of the taxpayer's net earnings or loss;
- (ii) Is from a pass-through entity which is subject to and files a return for the tax imposed by this part;
- (iii) Is allocated to a partner, shareholder, beneficiary or other owner of such pass-through entity; and
- (iv) Is not added to the net earnings or loss of such pass-through entity under item (J).

(J) Any net loss or item of expense or loss of a pass-through entity to the extent that such net loss or item of expense or loss is included in the federal taxable income or loss of a real estate investment trust which owns an interest in such pass-through entity either directly or indirectly through one (1) or more such entities and which files a return for the tax imposed by this part.

SECTION 3. Tennessee Code Annotated, Section 67-4-2006(b)(2), is amended by deleting item (K) in its entirety and by substituting instead the following new items:

- (K) Any net gain or any item of income which meets all of the following criteria:
- (i) Is included in the determination of the taxpayer's net earnings or loss;
 - (ii) Is from a pass-through entity which is subject to and files a return for the tax imposed by this part;
 - (iii) Is allocated to a partner, shareholder, beneficiary or other owner of such pass-through entity; and
 - (iv) Is not subtracted from the net earnings or loss of such pass-through entity under item (L).

(L) Any net gain or item of income of a pass-through entity to the extent that such net gain or item of income is included in the federal taxable income or loss of a real estate investment trust which owns an interest in such pass-through entity either directly

or indirectly through one (1) or more such entities and which files a return for the tax imposed by this part.

SECTION 4. Tennessee Code Annotated, Section 67-4-2012, is amended by deleting the last sentence of subsections (b), (e) and (g), and by adding a new subsection (k), as follows:

(k) For purposes of this section, property, payroll and receipts shall include a taxpayer's share of any specific property, payroll and receipts of a pass-through entity in proportion to such taxpayer's share of the federal taxable income or loss of such pass-through entity; provided, that there shall be no inclusion of such factors if any items of income, gain, deduction, loss or expense of such pass-through entity are excluded from the computation of the taxpayer's net earnings or loss pursuant to Sections 67-4-2006(b)(1)(I) or 67-4-2006(b)(2)(K).

SECTION 5. Tennessee Code Annotated, Section 67-4-2105(a), is amended by adding immediately after the language "Section 67-4-2008" the words "or under the provisions of subsection (b)".

SECTION 6. Tennessee Code Annotated, Section 67-4-2105, is amended by adding the following as a new subsection (b), and by relettering the existing subsection (b) and subsequent subsections accordingly:

(b) There shall be exempt from the payment of the franchise tax levied under this part an entity that is treated as a partnership for federal income tax purposes and that is wholly owned, directly or indirectly, by a real estate investment trust. In the event that such an entity is partly owned, directly or indirectly, by a real estate investment trust, the entity shall be exempt from the tax imposed by this part only to the extent that it is owned by a real estate investment trust. Such an entity shall file a franchise tax return as required by this part and compute the franchise tax as though it were not partially exempt. The franchise tax so computed shall then be multiplied by the percentage of

ownership by entities that are not real estate investment trusts and the result shall be the franchise tax payable by the entity for its tax year.

SECTION 7. Tennessee Code Annotated, Section 67-4-2108(a), is amended by deleting subdivision (1) in its entirety and substituting instead the following:

(1) The measure of the tax hereby levied shall in no case be less than the actual value of the real or tangible property owned or used in Tennessee, excluding exempt inventory. Notwithstanding the foregoing, in the case of an entity which is treated as a partnership for federal tax purposes (excluding S corporations) and in which a real estate investment trust directly or indirectly owns a majority of the total interests in partnership capital and profits, the sole franchise tax measure shall be net worth computed in accordance with the provisions of § 67-4-2106.

SECTION 8. Tennessee Code Annotated, Section 67-4-2111, is amended by deleting subsections (b)(2), (e)(3) and (g)(2) and by adding a new subsection (k), as follows:

(k) For purposes of this section, property, payroll and receipts shall include a taxpayer's share of any specific property, payroll and receipts of a pass-through entity in proportion to such taxpayer's share of the federal taxable income or loss of such pass-through entity; provided that there shall be no inclusion of such factors if any items of income, gain, deduction, loss or expense of such pass-through entity are excluded from the computation of the taxpayer's net earnings or loss pursuant to Sections 67-4-2006(b)(1)(I) or 67-4-2006(b)(2)(K).

SECTION 9. This act shall take effect upon becoming law, the public welfare requiring it, and shall apply to tax years ending on or after the date of this act, provided that the provisions of this act shall not take effect as to any tax year of an entity which is not subject to the provisions of Chapter No. 406 of the Public Acts of 1999.